

No. 10386

**In the United States Circuit Court of Appeals
for the Ninth Circuit**

PACIFIC POWER & LIGHT COMPANY AND AMERICAN
POWER & LIGHT COMPANY, PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT

BRIEF FOR THE RESPONDENT

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v.

FEDERAL POWER COMMISSION, RESPONDENT

BRIEF FOR RESPONDENT

COUNTERSTATEMENT OF THE CASE

This is a review, under Section 313 (b) of the Federal Power Act (49 Stat. 847), U. S. C., Title 16, § 825l (b), of Paragraphs (B) and (H) of the Federal Power Commission's order of November 24, 1942, requiring Pacific Power & Light Company¹ to correct its electric plant accounts in accordance with the Commission's Uniform System of Accounts, heretofore considered and approved by this Court in *Northwestern Electric Company v. Federal Power Commission*, 125 F. (2d) 882, and *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740.²

¹ Pacific Power & Light Company is sometimes hereinafter referred to as "Pacific", American Power & Light Company as "American" and Pacific and American as "Petitioners."

² A petition for certiorari to review this decision is now pending, No. 195, Oct. Term, 1943.

Paragraph (B) of the Commission's order requires that Pacific eliminate a \$4,121,981.41 "write-up" from its accounts by charging \$1,135,113.91 to a special reserve heretofore created for that purpose,³ and by charging the balance of \$2,986,867.50 to surplus—either earned surplus or capital surplus as Pacific may elect (1 R. 61-62). There is no dispute with respect to the entire amount of \$4,121,981.41 being a "write-up" and as such it has been transferred by Pacific to Account 107, Electric Plant Adjustments, where it became subject to disposition "as the Commission may approve or direct" (Pet. Br. 11; 1 R. 61, 63-64; 2 R. 565-569). Petitioners object, however, to the disposition of the "write-up" prescribed by the Commission and advance substantially the same contentions as those considered and rejected by this Court when it affirmed a similar order in *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740.

Paragraph (H) of the Commission's order here under review provides for the amortization of an amount of \$2,741,591.66 by annual charges to income over a ten-year period beginning in 1942 (1 R. 62-63). This amount is the portion of the acquisition cost to Pacific of certain utility systems which is in excess of the original cost of such systems (1 R. 157, 158, 168-176; 2 R. 440; 3 R., Ex. 17, Revised Statement B, pp. 17-14). This excess admittedly represented payment for "intangibles" such as going value, good will, nuisance value, franchise value, etc., and was essentially a

³ This reserve was created by Pacific for this purpose pursuant to a prior order of the Commission in another, but related, proceeding. *Pacific Power & Light Company et al.*, 2 F. P. C. 508, 511, 514-515; 42 P. U. R. (N. S.) 36, 39-40, 43.

capitalization of prospective earning power (Pet. Br. 16, 21, 22; 2 R. 391-393, 395, 400, 492-494, 514, 529-531). In accordance with the Uniform System of Accounts, Pacific has transferred the amount of \$2,741,591.66 to Account 100.5, Electric Plant Acquisition Adjustments, where it became subject to being "depreciated, amortized, or otherwise disposed of, as the Commission may approve or direct." Petitioners object to the ten-year amortization period prescribed by the Commission, but they recognize that the amount should not be retained permanently in Pacific's accounts, in which it has already lodged for as much as thirty-three years (Pet. Br. 3, 12, 14, 19; 1 R. 194; Appendix A of this brief, p. 38).

The issues on this review are therefore limited to the disposition of the \$4,121,981.41 "write-up" from Account 107, Electric Plant Adjustments, and the amortization of the \$2,741,591.66 of intangibles from Account 100.5, Electric Plant Acquisition Adjustments, prescribed in Paragraphs (B) and (H), respectively, of the Commission's order of November 24, 1942.

The uniform system of accounts

Against the background of information developed by the Federal Trade Commission's seven-year investigation of the utility industry⁴ which revealed the

⁴ In 1928, pursuant to Senate Resolution, the Trade Commission had undertaken a sweeping investigation of the public utility industry. The report of the Trade Commission fills 101 volumes. *Utility Corporations*, Sen. Doc. No. 92, 70th Cong., 1st Sess., 1935. This has been called "the most thoroughgoing investigation of an American industry that has ever appeared." Barnes, *The Economics of Public Utility Regulation* (1942), p. 71.

deficient and obscure accounting practices of utilities, Congress enacted the Federal Power Act, in which it conferred comprehensive accounting authority upon the Commission to meet and correct these deficiencies and to prevent their recurrence. *Section 301 (a)*.⁵

Prior to adoption of the Commission's Uniform System of Accounts, inflation and "write-ups" had been buried in the accounts, all the utility plant being frequently included in a lump-sum account so that it was impossible to ascertain the investment applicable to gas, electric, and other departments, much less the cost of generating stations, transmission lines, and other items of electric plant; and purchases made many years before were carried in one account from year to year without change in the amount recorded.⁶ Such conditions were, of course, detrimental to the investor and the consumer, and effective regulation, of which accounting, it has been truly said, is the heart-blood, was seriously impaired.⁷

⁵ This section authorizes the Commission to "prescribe a system of accounts to be kept by licensees and public utilities" and after "notice and opportunity for hearing" to "determine by order the accounts in which particular outlays and receipts shall be entered, charged, or credited." That section further provides that "The burden of proof to justify every accounting entry questioned by the Commission shall be on the person making, authorizing, or requiring such entry."

⁶ Federal Power Commission, *Twentieth Annual Report to Congress* (1940), p. 53; Tr. 1993-1994, Ex. 51. [Portions of the record certified but not printed will be cited as "Tr. 00" in accordance with a stipulation between counsel dated May 14, 1943, which stipulation is on file with this Court.]

⁷ Wilson, Herring, and Eutsler, *Public Utility Regulation* (1938), pp. 74-78; American Bar Association, Section of Public Utility Law, *Report by Committee on the Standards of Account-*

Having in mind these abuses and deficiencies, and in the light of the Congressional intent expressed in the Federal Power Act, the Commission undertook the preparation and promulgation of its Uniform System of Accounts. After the closest cooperation of a committee of the National Association of Railroad and Utilities Commissioners (N. A. R. U. C.) and of other State and Federal agencies, submission of the tentative draft to the State Commissions and to representatives of electric utilities, and receipt and consideration of all views and criticisms, the Commission prescribed its "Uniform System of Accounts for Public Utilities and Licensees." Federal Power Commission, *Sixteenth Annual Report to Congress* (1936), pp. 9, 10, 11; Tr. 1070, Ex. 1.⁸

One of the principal provisions of the Commission's System of Accounts (also contained in the system adopted by the N. A. R. U. C.) is the requirement that the utilities reclassify their electric plant accounts by prescribed accounts on the basis of original cost, that is, the cost of operating units or systems to the person

ing Prescribed for Public Utilities by Federal and State Authorities (1931), p. 7.

⁸ At or about the same time, the N. A. R. U. C. adopted a uniform system of accounts almost word for word the same as the Commission's, endorsed the Commission's system to the State Commissions, and recommended the use of either the Commission's or the N. A. R. U. C.'s system. Of the 42 regulatory commissions having jurisdiction over electric companies, 20 have prescribed the system adopted by the N. A. R. U. C. for use by electric companies subject to their jurisdiction, 16 have prescribed the Federal Power Commission's and the remaining 6 have prescribed modifications of the two systems. Moody's, *Public Utilities* (1943), page a38; see also Tr. 1993-1994, Ex. 51.

first devoting them to public service. The excess of book cost over original cost thus disclosed must be transferred to two adjustment accounts (Tr. 1070, Ex. 1, p. 19).

The portion of the excess representing "write-ups" or inflation must be placed in Account 107, Electric Plant Adjustments⁹ where it becomes subject to disposition "as the Commission may approve or direct."

The excess over original cost representing acquisition costs incurred in arm's-length transactions is placed in Account 100.5, Electric Plant Acquisition Adjustments,¹⁰ with a showing as to the nature of the excess, i. e., whether it represents going value, structural value, etc. These amounts are thereafter to be "depreciated, amortized, or otherwise disposed of, as the Commission may approve or direct" in the light of their nature and the applicable accounting principles (Tr. 1109, Ex. 5, p. 2).

As heretofore stated, this Court has reviewed and approved the Uniform System of Accounts prescribed by the Commission. *Northwestern Electric Company*

⁹ The text of Account 107 (Tr. 1070, Ex. 1, p. 19) provides that "Write-ups of electric plant prior to the effective date of this system of accounts shall be recorded herein" and "shall be disposed of as the Commission may approve or direct."

¹⁰ The text of Account 100.5 (Tr. 1070, Ex. 1, p. 19) provides that the difference between "the cost to the accounting utility of electric plant acquired as an operating unit or system" and the "original cost" is to be classified therein "according to the character of the amounts" and "shall be depreciated, amortized, or otherwise disposed of, as the Commission may approve or direct."

The provisions of Account 100.5 and Account 107 of the Commission's System of Accounts (Tr. 1070, Ex. 1, p. 19) and the provisions of the N. A. R. U. C. Accounts 100.5 and 107 (Tr. 2018, 2019, Ex. 51) are *in totidem verbis*.

v. *Federal Power Commission*, 125 F. (2d) 882, 886-7, and *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740, 741.

History of proceedings

Pursuant to the requirements of the System of Accounts, Pacific, which is admittedly subject to the Act as a "public utility" (Pet. Br. 4; 1 R. 92; 2 R. 403-404), submitted its purported reclassification and original cost studies to the Commission on July 3, 1940 (3 R., Ex. 15).¹¹ The results of a joint investigation of such studies by the staff of the Federal Power Commission and the staff of the Public Utilities Commissioner of Oregon¹² were embodied in a joint report (3 R., Ex. 16) which was served on Pacific with an order of the Commission (1 R. 1-5) directing Pacific to show cause at a public hearing why it should not be required, *inter alia*, to correct its studies and make the accounting adjustments recommended in the joint report; as well as submit plans for disposition of the amounts which should be classified in Account 107, Electric Plant Adjustments, and Account 100.5, Electric Plant Acquisition Adjustments.

After Pacific had filed its revised studies (3 R. Ex. 17), extended hearings were held, at which American,

¹¹ Under accounting requirements of the Oregon Commissioner (Tr. 1617, Ex. 49) and the Department of Public Service of Washington (Tr. 1991, Ex. 51), similar to those of the Federal Power Commission, Pacific filed identical studies with these state regulatory bodies (1 R. 118, 119).

¹² Examination of Pacific's studies was made jointly by the staff of the Commission and the staff of the Oregon Commissioner with the assistance, through consultation, of the staff of the Washington Commission (2 R. 405-406, 484).

Pacific's parent company, was permitted to intervene (1 R. 112 through 3 R. Ex. 17)..¹³

Following the submission of briefs, the Commission adopted its Opinion No. 84 (1 R. 36-60; 46 P. U. R. (N. S.) 131) finding that the \$4,121,981.41 "is properly classifiable in Account 107, Electric Plant Adjustments" as "a write-up of electric plant" (1 R. 47) which was recorded in Pacific's books of account as a result of transfers of certain properties to Pacific in 1910 and 1930 by American, which completely controlled and dominated Pacific (1 R. 42), that these transfers were under circumstances in which there was a "complete absence of arm's-length bargaining and of independence of judgment" (1 R. 43) and that they represented "nothing more than American dealing with itself" (1 R. 44).

Regarding disposition of the "write-up" the Commission said (1 R. 47):

* * * The provisions of Account 107 require the amounts recorded therein to be disposed of as we may approve or direct. We hold that, in accordance with sound principles of accounting, the amounts should be expunged immediately. We now turn to a consideration of disposition.

In Opinion No. 69, adopted on December 9, 1941, we approved, subject to certain conditions, the merger of Inland Power & Light

¹³ American, the Oregon Commissioner and the Washington Commission were granted leave to intervene in the hearing (1 R. 10, 14, 15). Honorable Ormond R. Bean, at that time Public Utilities Commissioner of Oregon, presided jointly with the Trial Examiner of the Commission at the hearing (1 R. 38).

Company with and into Pacific. In our order we required Pacific to set up a special reserve in the amount of \$1,135,113.91, being an amount by which the cost to Inland of the net assets transferred to Pacific exceeded Pacific's cost of the stock of Inland. We said in Opinion No. 69 that this "reserve shall be used only for such purposes as this Commission may subsequently approve or direct." The transactions giving rise to the reserve are associated with transactions giving rise to the amount of \$4,121,981.41 classifiable in Account 107. We accordingly find that \$1,135,113.91 of the \$4,121,981.41 should be charged to this special reserve.

We direct that the balance of \$2,986,867.50 (\$4,121,981.41 less \$1,135,113.91) be charged to Earned Surplus; provided, however, that Pacific may at its election charge all or any part of the said \$2,986,867.50 against a Capital Surplus properly created for such purpose.

With respect to the \$2,741,591.66, which Pacific classified in Account 100.5, Electric Plant Acquisition Adjustments, the Commission found that this amount "represent(ed) payment for intangibles" (1 R. 49) acquired "as far back as 1910" which "have been carried on Pacific's books all those years without any provision having been made, as good accounting practice demands, for writing off any part thereof" (1 R. 51). The Commission further found that the amounts representing these intangibles "should not be permitted to rest permanently in the accounts of a public utility" (1 R. 49) and should, in this case, be amortized over a "period of ten years, beginning with 1942" by "equal

annual charges * * * to Account 537, Miscellaneous Amortization" (1 R. 51).¹⁴

The order of November 24, 1942 (1 R. 61-64), accompanying the Commission's Opinion No. 84, provided in Paragraph (B), that Pacific should dispose of the \$4,121,981.41 "write-up" from Account 107, Electric Plant Adjustments, by charging \$1,135,113.91 to a special reserve heretofore created for that purpose and by charging the balance of \$2,986,867.50 to surplus—either earned surplus or capital surplus as Pacific may elect. The order further provided, in Paragraph (H), that Pacific should amortize the \$2,741,591.66 of "intangibles" from Account 100.5, Electric Plant Acquisition Adjustments, by annual charges to income over a ten-year period beginning in 1942 (1 R. 62-63).

Applications for rehearing filed by Pacific and American (1 R. 64-79) were denied by the Commission (1 R. 80-81) and a petition for review was thereupon filed in this Court on March 11, 1943.¹⁵

STATUTES INVOLVED

Pertinent excerpts from the Federal Power Act ^{act} ~~as~~ set forth in the Appendix to this brief.

¹⁴ The text of Account 537 provides that it "shall include" such "amounts as the Commission may, by order, require to be included herein, such as amortization of amounts in Account 100.5, Electric Plant Acquisition Adjustments" (Tr. 1070, Ex. 1, p. 94).

¹⁵ Rehearing and review had also been sought with respect to Paragraph (A) of the Commission's order requiring the \$4,121,981.41 to be classified in Account 107 as a "write-up", but on August 12, 1943, just prior to the due date of petitioners' brief herein, Pacific complied with this provision of the Commission's order (see 2 R. 565-569).

SUMMARY OF ARGUMENT

The Commission's finding that the \$4,121,981.41 is a "write-up" is clearly supported by substantial evidence and is no longer disputed by Pacific which has transferred this amount to Account 107, Electric Plant Adjustments, where it became subject to disposition "as the Commission may approve or direct." The disposition of the "write-up" to a special reserve and to surplus prescribed by the Commission is likewise supported by substantial evidence. Petitioners have proposed no "possible alternative * * * although the opportunity to do so has been long open" (*Alabama Power Co. v. Federal Power Commission* (App. D. C.), 128 F. (2d) 280, 295-296, *cert. denied*, 317 U. S. 652), and on this review they merely advance the same objections which this Court considered and rejected in affirming a similar order in *Northwestern Electric Co. v. Federal Power Commission*, 134 F. (2d) 740.

Pacific transferred \$2,741,591.66 to Account 100.5, Electric Plant Acquisition Adjustments, as the portion of the acquisition cost to Pacific of certain utility systems which was in excess of the original cost of such systems. This excess admittedly represented payment for "intangibles" such as going value, goodwill, nuisance value, etc., and was essentially a capitalization of prospective earning power. (*Cf., Niagara Falls Power Co. v. Federal Power Commission* (C. C. A., 2nd), —F. (2d) —, decided July 29, 1943).

The Commission's finding that such "intangibles" should be amortized by annual charges to income over a ten-year period beginning in 1942 is clearly supported by substantial evidence and the accounting authorities. These "intangibles" admittedly should not remain permanently in Pacific's accounts, in which they have already lodged for some twenty to thirty years.

Petitioners' belated objection that the amortization should be made through Account 505, Amortization of Electric Plant Acquisition Adjustments, as an operating expense, instead of Account 537, Miscellaneous Amortization, as an income deduction, is without merit. In this proceeding, which is admittedly not a rate case, "The label is unimportant, whether depreciation or amortization, if the substance of allowance is adequately preserved" (*American Telephone & Telegraph Co. v. United States*, 299 U. S. 232, 244). Moreover, the amount of income available for surplus is the same whether the amortization is through Account 537 or Account 505.

If the result of the Commission's order is to divert earnings which would otherwise be available for dividends, such result flows from the legitimate exercise of the Commission's accounting authority. *Northwestern Electric Company v. Federal Power Commission* (C. C. A. 9, 1943), 134 F. (2d) 740, 744-745; *Kansas City So. Ry. v. United States*, 231 U. S. 423, 453, 455.

ARGUMENT

I

The Federal Power Commission is clearly authorized to require Pacific to eliminate the "write-up" from its accounts

Pacific no longer objects to the Commission's finding that the amount of \$4,121,981.41 is a "write-up" and on August 12, 1943, it transferred this amount to Account 107, Electric Plant Adjustments¹⁶ (Pet. Br. 3, 43; 2 R. 565-569). The facts surrounding the "write-up" may therefore be summarized without extended discussion.

Some time late in 1909 or the early part of 1910, American turned its attention to the Pacific Northwest and began the acquisition of utility properties in that territory (2 R. 276). Through the acquisition of capital stock, it acquired control of various utility properties in the Yakima Valley (2 R. 276, 414-415). When it had succeeded in acquiring control of these utility properties, American caused the incorporation of Yakima-Pasco Power Company in March 1910, and of Columbia Power & Light Company in April 1910, to serve "as a temporary gathering place for [these] properties which [American] expected to turn over" to Pacific, which had not yet been formed (2 R. 274, 275, 276, 414, 415). The properties acquired in the Yakima Valley, with the exception of those of Astoria Electric Company, were at the instance of American, then transferred to Yakima-Pasco and Columbia com-

¹⁶ Account 107 provides that "write-ups of electric plant" shall be recorded therein and thereafter "disposed of as the Commission may approve or direct" (Tr. 1070, Ex. 1, p. 19).

panies (2 R. 276). The properties of Astoria Electric Company, an isolated electric system in the State of Oregon, remained in that corporate organization until all of the properties were finally transferred to Pacific (2 R. 276-277).

“After having assembled [these] properties for operation by Pacific” (1 R. 222; 2 R. 274, 414), American caused the incorporation of Pacific under the laws of Maine on June 16, 1910 (1 R. 128, 221, 222; 2 R. 274, 414, 415), and caused Yakima-Pasco, Columbia, and Astoria companies, through a nominee of American, to transfer their properties to Pacific (1 R. 93, 159-167; 2 R. 414).

In return for these properties, American had Pacific deliver to it \$5,997,000 par value of common stock, \$1,250,000 par value of preferred stock, \$3,200,000 principal amount of bonds and certain other minor obligations (2 R. 415). To balance the securities and other obligations issued to American, Pacific recorded the properties, costing American \$6,154,251.34, on its books at \$10,900,000, or \$4,745,748.66 in excess of American's *bona fide* cost incurred in arm's-length transactions¹⁷ (2 R. 277, 279, 280, 281, 439).

Upon receipt of these securities, American, in accordance with its predetermined plan, sold the bonds and preferred stock to the public, retaining the common stock which it still owns (2 R. 224).

¹⁷ In 1930, American transferred to Pacific certain properties of its wholly owned subsidiary, Inland Power & Light Company, at a recorded cost to Pacific of \$623,767.25 less than actual cost to American. The effect of this transfer was to reduce the excess of recorded cost to Pacific over cost to American involved in the 1910 transfer to the net figure of \$4,121,981.41 (2 R. 428-431).

Upon consideration of the overwhelming evidence that American had controlled Astoria Electric Company; had organized, controlled, and dominated Yakima-Pasco Power Company, Columbia Power & Light Company, and Pacific; and had caused the organization of the companies and the transfers of the property as part of a predetermined and preconceived plan, developed by American, in which the amount Pacific was to pay for the properties had been decided by American even before Pacific was in existence, the Commission found that the "amount of \$4,121,981.41 is a write-up of electric plant * * * classifiable in Account 107, Electric Plant Adjustments"¹⁸ (1 R. 47) finding that there was a "complete absence of arm's-length bargaining and of independence of judgment" in the 1910 transfer (1 R. 43); that "the transaction represented nothing more than American dealing with itself" (1 R. 44); that the "buyers and sellers" were "mere tools of the holding company" (1 R. 44) and that "no one in good conscience could make the claim that the excess of \$4,121,981.41 represents actual bona fide cost" (1 R. 44).

Based upon the uncontroverted expert testimony of two of its principal accounting officers that the "write-

¹⁸ For the details of this evidence see the record at pages 1 R. 93, 128, 221-224, 226, 227-231, 233, 238-242, and 272; 2 R. 273-276, 282, 298-299, 301-302, 323, 325-327, 347-348, 385, 388, 414-415; and Exhibits 20 (1 R. 159-167), 22 (1 R. 243-245), 32 (2 R. 294-297), 33 (2 R. 350, 361), and 34 (2 R. 369-371). In the light of the overwhelming and conclusive evidence on this point, "It is difficult to see how the Commission could have found otherwise." *Puget Sound Power & Light Co. v. Federal Power Comm.* (App. D. C., decided August 23, 1943) — F. (2d) —.

up" should be eliminated from the accounts of Pacific, in accordance with sound principles of accounting, by a charge to Earned Surplus or Capital Surplus (2 R. 488, 534), the Commission directed the elimination of \$1,135,113.91 of the "write-up" to a special reserve created by Pacific for such purpose (1 R. 47, 61) and of \$2,986,867.50 of the "write-up" by a charge to Earned Surplus, with the proviso that Pacific at its election may charge all or any part of the latter amount to a capital surplus properly created for such purpose (1 R. 48, 61-62).

Petitioners do not contend that the Commission's method of disposition of the "write-up" is not supported by substantial evidence (Pet. Br. 42-45).¹⁹ Moreover, since all amounts transferred to Account 107 become subject to disposition "as the Commission may approve or direct," the Commission's authority to dispose of the "write-up", as distinguished from the method of such disposition, is not properly in issue. *American Tel. & Tel. Co. v. United States*, 299 U. S. 232, 240. Assuming, however, *arguendo*, that the question may now be raised, the authority of the Commission to require such disposition has been settled in *Northwestern Electric Company v. Federal*

¹⁹ Not only is the method of disposition directed supported by uncontroverted and substantial evidence, but, in addition, Pacific has not proposed any other plan of disposition of the "write-up." Having made "no suggestion of any possible alternative to that proposed by the Commission, although the opportunity to do so has been long open" Pacific is now precluded from questioning "the propriety of the order." *Alabama Power Co. v. Federal Power Comm.* (App. D. C.), 128 F. (2d) 280, 295-296, *cert. den.* 317 U. S. 652.

Power Commission, 125 F. (2d) 882, and *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740, and by the unanimous decisions of other Courts.²⁰

The *Northwestern* cases likewise dispose of petitioners' contentions that the Commission is without authority "to require the elimination from the asset side of the balance sheet of a public utility of any sum fully supported by the present fair value of its assets" (Pet. Br. 15, 43-44); that the Commission erred in "ignoring, and in refusing to permit the introduction of" evidence "which fully establishes [that] the fair value of Pacific's assets is equal to or in excess of the recorded book value thereof" as "immaterial and irrelevant" (Pet. Br. 15); and that the Commission's authority to eliminate the "write-up" is not retroactive (Pet. Br. 15).

Petitioners are unable to distinguish this case from the *Northwestern* cases. Under the principle of *stare decisis* an extended discussion of petitioners' conten-

²⁰ *Louisville Gas & Electric Co. v. Federal Power Commission* (C. C. A. 6th), 129 F. (2d) 126, *cert. den.*, February 8, 1943, No. 616, Oct. Term, 1942; *Alabama Power Co. v. Federal Power Commission* (App. D. C.), 128 F. (2d) 280, *cert. den.* 317 U. S. 652; *Northern States Power Co. v. Federal Power Commission* (C. C. A. 7th), 118 F. (2d) 141. The Commission is authorized by Section 301 (a) of the Act to prescribe a system of accounts with which every public utility and licensee is required to comply, and which carries with it the authority to require proper accounting adjustments. *American Tel. & Tel. Co. v. United States*, 299 U. S. 232, 240; *Norfolk & Western Ry. Co. v. United States*, 287 U. S. 134, 141; *Kansas City So. Ry. Co. v. United States*, 231 U. S. 423, 440; *Long Beach Gas Co. v. Maltbie*, 36 N. Y. S. (2d) 194, 203-204, *affirmed* 48 N. E. (2d) 167.

tions respecting the relevancy of "value" evidence therefore does not appear to be necessary or appropriate. *Jaffe v. Federal Trade Commission* (C. C. A. 7th, 1941), 123 F. (2d) 814; *Grand Rapids & I. R. Co. v. Blanchard* (C. C. A. 6th, 1930), 38 F. (2d) 470.

The following quotations from this Court's opinion in *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740, are particularly pertinent:

This is the second chapter of the story of a controversy between Northwestern Electric Company, petitioner, and the Federal Power Commission. We first considered the conflict in *Northwestern Electric Co. v. Federal Power Comm'n.*, 9 Cir., 125 F. (2d) 882. As there stated the Federal Power Act authorizes the Commission to prescribe a system of accounts. On the first review we sustained the power of the Commission to prescribe the system of accounts it did prescribe. That system requires accounts to show the original cost of the assets (p. 741).

* * * * *

The arguments that the actual values of petitioner's business has been ignored by the Commission are not pertinent. On the first review we approved the system of accounts prescribed, and we will not revive the arguments (p. 744).

* * * * *

Petitioner also contends that the order is arbitrary and capricious because: * * *

(4) [It ignores] the actual values of petitioner's properties. The first and fourth of these rea-

sons are not pertinent because they have no bearing on the "original cost" theory of the system of accounts (p. 744).

II

The amortization of the "intangibles" prescribed by the Commission is fully supported by substantial evidence

Pacific has classified \$2,741,591.66 in Account 100.5, Electric Plant Acquisition Adjustments. This amount had its origin in fifteen acquisitions of property by Pacific, nine acquisitions having occurred in 1909-1911, some thirty-three years ago; three in 1915-1916, some twenty-seven years ago; one in 1923, some twenty years ago; and two, involving insignificant amounts, in 1928 and 1935.²¹

Practically all of the \$2,741,591.66 relates to two transactions which took place some twenty and thirty-three years ago. During this long period none of this amount has been depreciated, amortized or otherwise disposed of, although, as admitted by Pacific, much of the property acquired has been rebuilt, expanded, changed or retired to such an extent that it is not now possible to identify fully whatever portion of the acquired property is still in existence (3 R., Ex. 15, p. 118; Ex. 17, Revised Statement B, p. 37).²²

²¹ Facing page 38 of this brief, as Appendix A, we have printed in tabulation form a detailed analysis of this amount. The tabulation can be unfolded and read in connection with the text of the brief.

²² The properties were, in many instances, in existence long before they were acquired by Pacific. They go back as far as 1885 and passed through several ownerships prior to acquisition by Pacific (e. g., 1 R. 128, 157; Ex. 15, p. 23; 3 R., Ex. 17, Revised Statement B, pp. 16, 17, 37, 38-40).

Petitioners concede that the \$2,741,591.66 excess of acquisition cost over original cost represented a payment by Pacific for intangibles (Pet. Br. 16, 21, 22). Moreover, petitioners describe the properties acquired as "local steam and small hydro-electric generating and distribution systems, which, in general, had developed from makeshift beginnings in connection with saw-mills, flourmills and other enterprises of a similar nature, which were valuable going concerns in 1910, but were not, generally speaking, efficiently equipped with adequate generating and distributing facilities, from the standpoint of the art as then developed" (Pet. Br. 6, 7).

At the hearing, Pacific's witness Will T. Neill, Vice-President of Pacific, and the Commission's expert witnesses, Mr. Charles W. Smith, Chief of the Bureau of Accounts, Rates and Statistics and Mr. Melwood W. Van Scoyoc, Chief of the Commission's Division of Original Cost, agreed that Pacific paid for intangibles (2 R. 391-392, 395, 400, 492-493, 529); that these intangibles included goodwill,²³ going value, nuisance value,²⁴ franchise value and, *inter alia*, monopoly value (2 R. 392, 393, 494, 514, 530-531); that the intangibles are rooted in and based upon the purchasers' evaluation

²³ In the opinion of petitioners' witness Neill, goodwill is a part of going value (2 R. 392). *Accord*, see: *The Law of Goodwill*, G. A. D. Preinreich, December 1936, 11 Acctg. Rev. 317, 325-326—"Franchise, going value, and goodwill are one and the same thing."

²⁴ Pacific concedes that "it is also fair to assume that the purchase price to Pacific" of Hydro-Electric Company, acquired in 1915 and involving \$115,718.63, "may have been influenced by and have included recognition of a 'nuisance value' of the properties in the hands of the original stockholders of Hydro-Electric Company" (3 R., Ex. 17, Revised Statement B, p. 11).

of "the prospective earning power of the situation",²⁵ (2 R. 392, 393, 494, 530-531); that all of these intangibles "tend to merge" and that "it would be highly speculative and an impractical thing to" divide them up, segregate or pigeon hole them (2 R. 393, 494, 530-531).

The Commission's finding, which is not contested, that the \$2,741,591.66 represented payment for intangibles, is therefore clearly supported by substantial evidence and is conclusive within the meaning of Section 313 (b) of the Act.²⁶

The Commission's finding that the amount should be amortized from Account 100.5, Electric Plant Acquisition Adjustments, by specified annual charges to income is similarly supported by the uncontroverted expert testimony of two of the principal accounting officers of the Commission.

Witness Van Scoyoc, whose qualifications were unquestioned, testified (2 R. 494-496):

Q. Do you believe that intangibles bought and paid for have a permanent place in the plant accounts of a public utility?

²⁵ As Judge Learned Hand pointed out in *Niagara Falls Power Company v. Federal Power Commission* (C. C. A. 2d, July 29, 1943), — F. (2d) —, "The only factor which determines its price (the price of a plant, built and in operation) is the 'prospective revenues' which it will produce."

²⁶ *Montana Power Company v. Federal Power Commission* (C. C. A. 9th, 1940), 112 F. (2d) 371, 374; *Northwestern Electric Company v. Federal Power Commission* (C. C. A. 9th, 1942), 125 F. (2d) 882, 887; *Rochester Telephone Corp. v. United States*, 307 U. S. 125, 146 (1939); and see also the concurring opinion of Judge Healy in *Northwestern Electric Company v. Federal Power Commission* (C. C. A. 9th, 1943), 134 F. (2d) 740, 745.

A. No, sir; I do not. Intangibles have a very questionable value, as well as life. There is no more reason to retain permanently the cost of an intangible in the books of account than there is to retain the cost of tangible property in the accounts after it has been physically retired. The difficulty lies in the fact that the life of an intangible is uncertain and its decline in value is not as easily ascertainable as that of tangible property. The sane and prudent thing for management to do is to provide for its ultimate loss in value. It is good accounting and it is practiced to a large extent by non-utility business enterprises. I might add that it is beginning to be practiced by a good many public utilities with which we have come in contact in our reclassification work.

Q. Do you have any specific recommendation with respect to the disposition of the amount in the acquisition adjustment account of \$2,741,-591.66?

* * * * *

A. * * * Yes. My recommendation would be that this amount be disposed of from Account 100.5 by equal annual charges to Account 537, over a period of 10 or 15 years commencing with the year 1941.

* * * * *

Q. Why do you recommend a 10 or 15-year amortization period?

A. While I believe a shorter period would be more desirable in view of the fact that approximately one-half of the acquisition adjustment has been carried on the books of the Company for 30 years, in matters of this kind a practical

solution is sought and, in my judgment, an amortization program of 10 or 15 years will satisfactorily accomplish the disposition of the acquisition adjustment.²⁷

Witness Charles W. Smith, whose qualifications as an expert accountant were also unquestioned, testified (2R. 530-532, 533):

A. The amounts which the staff recommends be included in Account 100.5 represent acquisitions made in 1910 and 1930, although the latter acquisitions go several years back of 1930 when the properties involved were purchased by an affiliated seller. Hence these intangibles have been on the books a long time. * * * They have no permanent place in the accounts of a public utility. * * * In my opinion all amounts in the plant accounts should be charged off some time. The cost of physical items should be removed when the properties with which they are associated are retired. Intangibles are evasive and disappear without being seen. We only perceive the result of their disappearance. Thus rapid charge-offs of intangibles are required, I believe, by good accounting, good management, and good regulation.

* * * * *

²⁷ Cf. Justice Black dissenting, *McCart v. Indianapolis Water Co.*, 302 U. S. 419, 436: "‘Intangibles’ * * * might well be defined as ‘properties’ that can neither be seen nor touched and which can rarely be understood. * * * These property concepts are so uncertain, tenuous, and elusive that no two witnesses give them the same value except on occasions when several witnesses have been employed by the same litigant." See also: Kester, Roy B., *Principles of Accounting* (1939), p. 573, commenting on "intangible nature of goodwill" and "its more or less speculative value."

The amounts I am discussing have been in the accounts of the Pacific Company for a very long time. The conditions under which the properties were bought will not go on forever. Changes are constantly taking place. New forces, new inventions, new economic conditions prevail. I think, therefore, that these amounts which have already rested in the accounts a very long time ought to be disposed of quickly. It is my opinion that they should be disposed of over a period not in excess of 10 or 15 years at the most.

* * * * *

Q. To what account should the amortization of amounts representing the cost of intangibles, included in Account 100.5, be charged if the Commission should approve an amortization plan such as you have suggested?

A. The amounts I believe should be amortized by charges to Account 537, Miscellaneous Amortization. I believe the best accounting practice is to charge off the cost of intangibles to the final section of the income statement, and Account 537 seems most appropriate in this connection.

Moreover, Pacific, which had the burden of proof (Section 301 (a)),²⁸ did not propose to retain the \$2,741,591.66 in Account 100.5, permanently, but only until “the complete retirement or disposition of the

²⁸ As was held by this Court in *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740, 743, Section 301 (a) of the Federal Power Act imposes upon the utility whose accounting entries have been questioned by the Commission, the “burden of going forward” with “substantial evidence” to “justify” such entries.

respective systems to which the components of this total respectively apply; and at such time or times to remove from Account 100.5 so much thereof as pertains to the system acquisitions then retired or disposed of" (1 R. 194) and further, "in the event of the complete retirement or disposition of any system representing less than the total of one of the several acquisitions" to apportion "the amount of the 100.5 acquisition adjustment cost applicable to the entire acquisition, in such manner and on such bases as will fairly reflect the relation of the systems so disposed of or retired to the total acquisition" (1 R. 194).

Pacific did not sustain its "burden of going forward" with "substantial evidence" to "justify" its plan of disposition, though it has had every opportunity to do so. The average life of steam-electric property is 31 years and of hydro-electric property, it is 40 years (*U. S. Treasury Department, Bureau of Internal Revenue, Bulletin "F", Revised January 1942, p. 61*). The property acquired by Pacific is as much as thirty-three years old. It should by this time have been substantially, if not entirely, retired. *Southern Colorado Power Company*, — S. E. C. —; S. E. C. File Nos. 54-55 and 59-51, Holding Company Act of 1935, Release No. 4501, August 24, 1943, pp. 25-26; *Ogden Corporation*, — S. E. C. —; S. E. C. File No. 54-69, Holding Company Act of 1935, Release No. 4307, May 21, 1943, p. 23. Moreover, the evidence indicates that the property with which the \$2,741,591.66 originated is no longer in existence. The record shows that it has been rebuilt, expanded,

changed, and retired to the point that Pacific is unable to say that any part of it still exists today (3 R., Ex. 15, pp. 31, 32, 46, 118; Ex. 17, Revised Statement B, p. 37). Thus, under any theory of the case the \$2,741,591.66 should be amortized and the Commission was very liberal in permitting Pacific another ten years within which to accomplish such amortization.

Contrary to petitioners' contention (Pet. Br. 20-26) the amortization of the intangibles prescribed by the Commission is fully supported by the accounting authorities.

The *Accountants' Handbook, Third Edition*, Paton (1943), pp. 850-851, clearly recognizes that it is in accordance with correct principles of accounting to amortize the cost of intangibles.²⁹ This is true even when they have a "present value", Sherwood, J. F., & Hornberger, D. J., *Fundamentals of Auditing*, (1933), p. 146. Also Kester, Roy B., *Principles of Accounting*, 1939, p. 573.

The amortization of intangibles is supported by Sanders, Hatfield, and Moore, in their *Statement of Accounting Principles* published in 1938 by the American Institute of Accountants. The anticipatory attempt of petitioners (Pet. Br. 23-25) to disparage "the writing off of amounts paid for intangibles [as] a principle of conservatism rather than accounting"

²⁹ Though the Handbook refers to Goodwill, that intangible "is the most important and typical intangible asset" and refers to "all the favorable attitudes impinging upon the concern" so that discussion of it serves for the group of intangibles. *Accountants' Handbook, Third Edition* (1943), pp. 845-846; *A Statement of Accounting Principles*, Sanders, Hatfield and Moore (1938), p. 67.

is without merit. As is indicated by the title, the writers were setting forth "*A Statement of Accounting Principles.*" They also state (at pages 68, 69) that though there "is a marked difference of opinion and practice as to whether or not goodwill should be written off" and that the "regular amortization of goodwill is not considered imperative", such a treatment "is not considered objectionable." For the purpose of administering the Federal Power Act, the Commission may, of course, choose that method of accounting which in its judgment is best fitted for the performance of its statutory duties. *American Telephone & Telegraph Co. v. United States* (D. C., S. D., N. Y.), 14 F. Supp. 121, 129; *aff'd* 299 U. S. 232; *Norfolk & Western Ry. Co. v. United States*, 287 U. S. 134, 141, 143.³⁰

Nor is it material that the Bureau of Internal Revenue may allow no deduction from taxable income (Pet. Br. 22) for "depreciation, including obsolescence, * * * in respect of goodwill." In the first place, the tax cases cited by petitioners (Br. 23) do not support their contention that the accounting practice prescribed by the Commission is unsound. Secondly, the rule for income-tax purposes has been said to be "seriously objectionable" (Paton's *Accountants' Handbook*, Third Edition, 1943, p. 851); and finally, the Board of Tax Appeals in *First National Bank of St. Louis*, 3 B. T. A. 807, 808-809, itself stated that "as we have heretofore had occasion to remark,

³⁰ The Commission's determination is one "informed by experience" and is entitled to great weight. *Virginian Ry. Co. v. United States*, 272 U. S. 658, 665-666.

the income tax laws are not always in accord with accounting practice." Cf. *Kansas City Southern Ry. v. Commissioner* (C. C. A., 8th, 1931), 52 F. (2d) 372, 378, *cert. den.* 284 U. S. 676 (1931); *Chesapeake & Ohio Ry. v. United States* (E. D. Va., 1933), 5 F. Supp. 7, 10.

Further support of the Commission's requirement that intangibles be amortized is found in the Interstate Commerce Commission's consistent practice of approving purchases of property, where the excess of purchase cost over cost to the seller represents a payment for intangibles, only upon the condition that the amount of intangibles be amortized or written off at once. *Crown Coach Company*, 36 M. C. C. 144, 147 (1940); *Herrin Transportation Company*, 25 M. C. C. 710, 712 (1939); *Buckingham Transportation Company of Colorado, Inc.*, 25 M. C. C. 667, 670 (1939); *Mason & Dixon Lines, Inc.*, 36 M. C. C. 475, 481 (1941); and a host of other cases cited at 25 M. C. C. 832.³¹

In *Re Illinois Power & Light Corporation*, P. U. R. 1928 A, 776, 779-780, the Illinois Commerce Commission approved an acquisition of property only upon condition that the excess of the purchase price over cost to the predecessor be amortized or written off at once and not be reflected in fixed capital accounts. That Commission held that while a prospective purchaser might feel warranted in paying such excess

³¹ And see *Re Tuolumne County Electric Power & Light Company* (California Railroad Commission), P. U. R. 1928 C, 31, 33-34; *Re California Tel. & Light Company* (California Railroad Commission), P. U. R. 1929 D, 221, 224; *Re Nevada, California & Oregon Tel. & Tel. Co.* (California Railroad Commission), P. U. R. 1929 D, 43, 49-50.

because he anticipated being able to develop the property beyond that realized by the seller thus increasing the net return, the inclusion of such excess in fixed capital was unwarranted and against the public interest.

The fact that these cases involved the approval of the acquisition of property does not distinguish them from the case at bar, since the principle is the same. They clearly hold that intangibles should not remain permanently in the plant accounts but should be amortized or written off at once. In *Herrin Transportation Company, supra*, the Interstate Commerce Commission stated that "The public interest requires that a carrier refrain from reflecting figures in its accounts likely to create a false impression, and we do not believe that we should approve a transaction under section 213 unless steps are to be taken to eliminate from the accounts any fictitious increase in assets represented by amounts paid for intangible property." And in *East Texas Motor Freight Lines*, 25 M. C. C. 779, 782, that Commission pointed out that its findings were conditioned to permit amortization of the intangible property account over a reasonable period of years "As an aid in fostering sound financial and economic conditions in the motor-carrier industry."

It is likewise significant that in conditioning its approvals upon the elimination of the intangibles, the Interstate Commerce Commission has clearly indicated that the accounting prescribed therefor is in accord with its uniform system of accounts. *System Freight Service*, 36 M. C. C. 601, 604-605 (1941); *Andrew B. Crichton et al.*, 25 M. C. C. 783, 785-787 (1939).

The experience of the Federal Power Commission in the administration of the Act further confirms the propriety of its method of amortizing intangibles from Account 100.5. As shown in Appendix B to this brief, the Commission, between November 1940 and September 1943, approved thirty-three voluntary applications from electric utilities proposing plans for amortization of amounts established in Account 100.5.³²

III

Petitioners' objections to the Commission's amortization of the "intangibles" are without merit

As heretofore stated, Pacific has transferred the \$2,741,591.66 of "intangibles" to Account 100.5, Electric Plant Acquisition Adjustments, where it became subject to being "depreciated, amortized, or otherwise disposed of, as the Commission may approve or direct." Petitioners do not, and validly could not, challenge the Commission's authority to prescribe such an account. *Northwestern* cases, *supra*. It is fully within the holding of the Supreme Court in *American Telephone & Telegraph Company v. United States*, 299 U. S. 232, sustaining a similar provision in the system of accounts of the Federal Communications Commission. The Court there held that the acquisition cost in excess of original cost could properly be disposed of "after the character of the item

³² During the eleven-year period 1929 to 1939, ninety-eight industrial concerns in the United States "voluntarily wrote off intangible assets on their books" to the extent of \$786,000,000. *Accounting for Intangible Assets*, Harold G. Avery, 17 Acctg. Rev. 354-363 (October 1942).

had been determined” and that such disposition “must depend upon evidentiary circumstances, difficult to define or catalogue in advance of the event” (pp. 240, 242).

In this proceeding, extended hearings were held and the origin and nature of the \$2,741,591.66 were fully explored and established. It admittedly represented “intangibles” and, as petitioners recognize, this amount cannot remain permanently in Pacific’s accounts (1 R. 194). The Commission’s finding that this amount should be amortized by annual charges to income over a ten-year period, beginning in 1942, is, as shown under Point II of this brief, fully supported by substantial evidence and in accord with correct principles of accounting.

Petitioners’ belated contention (Br. 27, 28, 39) that the amortization should have been through Account 505, Amortization of Electric Plant Acquisition Adjustments, instead of Account 537, Miscellaneous Amortization, is also without merit. Contrary to the express requirement of Section 313 (b) of the Act, this objection was not urged in petitioners’ applications for rehearing (1 R. 64, 68-70, 71, 76-77) or in the petition for review (1 R. 91, 103-104), and petitioners assign no grounds for their failure so to do.³³

Since the \$2,741,591.66 admittedly represented “intangibles,” which are essentially rooted in earning power, rather than tangible property which is utilized

³³ Section 313 (b) of the Act provides: “No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.”

in operations, the amortization is properly made through Account 537, as an income deduction, and not through Account 505, as an operating expense. This is clearly supported by the accounting authorities, Sherwood, J. F., & Hornberger, D. J., *Fundamentals of Auditing* (1933), p. 148; Greeley, Harold Dudley, *Theory of Accounts* (1920), Vol. I, p. 410; Kester, Roy B., *Principles of Accounting* (1939), p. 573; Sanders, Hatfield and Moore, *A Statement of Accounting Principles* (1938), p. 69. Moreover, the Interstate Commerce Commission has required the amortization of intangibles by charges to income or their immediate elimination by charges to surplus. (See cases cited at pp. 28, 29, supra.)

Whether the amortization is through Account 505 or Account 537 does not involve any deprivation or confiscation of property, since the amount of income available for surplus is not affected. This is demonstrated in Appendix C to this brief. We there have taken Pacific's income statement for the twelve months ending December 31, 1940, as reported to the Commission in Pacific's Annual Report (which is in evidence in this proceeding), and show that the same amount will be available for transfer to surplus whether the amortization is made through Account 505 or Account 537.

As petitioners recognize (Br. 42), after an extended discussion (Br. 26-29), this is not a rate case (2 R. 514-516), and under the Supreme Court decision in *American Telephone & Telegraph Company v. United States*, 299 U. S. 232, in this proceeding:

The label is unimportant, whether depreciation or amortization, if the substance of allowance is adequately preserved (p. 244).

See also *Norfolk & Western Ry. v. United States* (W. D. Va., 1931), 52 F. (2d) 967, 970, *aff'd.*, 287 U. S. 134 (1932); *State Corporation Comm. of Kansas v. Wichita Gas Co.*, 290 U. S. 561, 569 (1934); *United States v. Los Angeles & S. L. Ry.*, 273 U. S. 299 (1927); and *Northwestern Electric Company v. Federal Power Commission* (C. C. A. 9th, 1942), 125 F. (2d) 882, 886, for cases showing, *inter alia*, irrelevancy of rate case considerations in an accounting case such as the one at bar.

Petitioners further contend that the Commission erred in requiring the amortization of the excess over original cost if the "fair value" of Pacific's properties as of December 31, 1940, supports the book cost (Pet. Br. 27, 28, 31). This contention was first rejected in *Northwestern Electric Company v. Federal Power Commission*, 125 F. (2d) 882, 886, and again in *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740, 744, this Court saying "The arguments that the actual values of petitioner's business has been ignored by the Commission are not pertinent. On the first review we approved the system of accounts prescribed, and we will not revive the arguments. * * * [the actual values] have no bearing on the 'original cost' theory of the system of accounts."

Moreover, assuming its relevancy, the "fair value" evidence offered here was not competent or material to show that the "intangibles" paid for with the

\$2,741,591.66 are “supported by the present fair value of the property assembled as a whole” (Pet. Br. 27). Pacific’s counsel stated the relevancy of the “fair value” evidence as follows (1 R. 204):

It has no relation to those estimates or determinations [of the excess over original cost and original cost] whatsoever, except in the sense that it relates to the same property. *I mean, it does not undertake to have any definite relation to the original costs or purchase costs, or any other kind of costs; it is a straight presentation of the value of this property as of December 31, 1940 * * ** [Italics supplied.]

The “fair value” as of December 31, 1940, therefore is not competent or material to show that the intangibles purchased twenty to thirty-three years ago “cannot disappear” (Pet. Br. 21); that their “value” increases (Pet. Br. 21); that they have not disappeared; that they have a certain value today; or that they have “merely [lost] their identity by fusion with the system and situation of which they have become inseparable parts” (Pet. Br. 21, 22).

Petitioners’ statements, in their brief, that intangibles cannot disappear; have not disappeared; have increased in value; have merely lost their identity; and have fused with the tangible property, are unfounded and gratuitous assumptions and are without support in the record as is indicated by the absence of record references in petitioners’ brief (Pet. Br. 21, 22, 26, 27, 31). On the contrary intangibles such as those involved here, tend to and do disappear as witness the

street railways of which the same was said as petitioners say here of the electric industry (2 R. 506). There is no asset, with the possible exception of land, which is not subject to declining value and complete disappearance as a result of economic and other forces. In view of the fact that the properties purchased are virtually no longer in existence (3 R., Ex. 15, p. 118; Ex. 17, Rev. Statement B, p. 37), if the intangibles had fused with the tangible property and become an integral part thereof as contended by petitioners (Pet. Br. 22), then such intangibles disappeared with the property, which has been substantially, if not entirely depreciated,³⁴ and the excess cost applicable to them should likewise have been substantially, if not entirely amortized. *Accord*, Pet. Br. 22; *Southern Colorado Power Company*, — S. E. C. —; S. E. C. File Nos. 54-55 and 59-51, Holding Company Act of 1935, Release No. 4501, August 24, 1943, pp. 25-26; *Ogden Corporation*, — S. E. C. —; S. E. C. File No. 54-69, Holding Company Act of 1935, Release No. 4307, May 21, 1943, p. 23.

Petitioners also contend that the requirement that Pacific amortize the intangibles is an adjudication that the common stock of the company is not legally paid-up; that such a question is a judicial one to be determined by the courts and the law of the state of incorporation; and that the Commission has thus assumed judicial powers (Pet. Br. 41-42).

³⁴ The average life of steam-electric property is 31 years and of hydro-electric property, 40 years. *U. S. Treasury Department, Bureau of Internal Revenue*, Bulletin "F," Revised January 1942, p. 61.

These contentions were rejected by this Court in the second *Northwestern* case, *supra*, 134 F. (2d) 740, 744:

The act, however, authorizes the Commission to "determine by order the accounts in which particular outlays and receipts shall be entered, charged, or credited" 16 U. S. C. A. § 825 (a). The Commission was authorized to do what it did, regardless of whether the effects mentioned by petitioner result.

Finally, petitioners complain that the order confiscates their property because "earnings or surplus which would otherwise be available for the payment of dividends are used" for the amortization of the intangibles (Pet. Br. 31).

The same contention was disposed of in *Northwestern Electric Company v. Federal Power Commission*, 134 F. (2d) 740, 744-745, this Court saying:

Finally, it is argued that the order deprives petitioner of its property without due process of law. We previously held that petitioner was not deprived of the value of its properties without due process of law, 125 F. (2d) 882, 886. However, it is now said that the effect of the order is to make American again pay for stock which it bought on the open market in good faith, since the earnings became frozen in the capital of the corporation. In addition, computed at the present earning rate, it will be between ten and twenty years before the common stock will again be in the position so that dividends can be paid thereon. It is said, therefore, that while such an order might be valid as against the promoters, if they still held the

stock, it is highly unfair as against American, and that such order deprives it of the value of the stock and its normal right to dividends.

While it might be said that American is not entitled to the earnings until declared as dividends, and therefore nothing has been taken from it, that view disregards realities. It is certainly possible, if not probable, that the market value of the stock would decrease, probably substantially, if no dividends can be paid thereon for ten years or more. However, in *Kansas City So. Ry. v. United States*, 231 U. S. 423, 455, 34 S. Ct. 125, 58 L. Ed. 296, 52 L. R. A., N. S., 1, it was held that a railroad could be compelled to charge a disputed item against its earnings. The order involved here requires the same thing, and adopts the principle approved in the cited case. If a company can be compelled to charge an item against earnings, for one year, we see no reason why it cannot be compelled to make the same kind of entries for succeeding years.

If the result of the Commission's order is to divert earnings which would otherwise be available for dividends, such result flows from the legitimate exercise of the Commission's accounting authority. *Kansas City So. Ry. v. United States*, 231 U. S. 423, 453, 455.

CONCLUSION

In conclusion it is respectfully submitted that the Commission's order is fully supported by substantial and uncontradicted evidence³⁵ of expert accountants

³⁵ *Montana Power Co. v. Federal Power Commission* (C. C. A. 9th, 1940), 112 F. (2d) 371, 374.

and accords with established principles of correct accounting. In reviewing such order, the Court is not "at liberty to substitute its own discretion for that of administrative officers who have kept within the bounds of their administrative powers"³⁶ and "so long as there is warrant in the record for the judgment of the expert body it must stand."³⁷ Since the Commission's order is not "so entirely at odds with fundamental principles of correct accounting"³⁸ nor "so arbitrary and outrageous"³⁹ as to be the "expression of a whim rather than an exercise of judgment"⁴⁰ it should be affirmed.

Respectfully submitted.

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General Counsel,

REUBEN GOLDBERG,
Senior Attorney,

Counsel for Respondent, Federal Power Commission.

SEPTEMBER 1943.

³⁶ *American Tel. & Tel. Co. v. United States*, 299 U. S. 232, 236 (1936).

³⁷ *Rochester Tel. Corp. v. United States*, 307 U. S. 125, 145-146.

³⁸ *Kansas City S. R. Co. v. United States*, 231 U. S. 423, 444 (1913).

³⁹ *Norfolk & Western Ry. v. United States*, 287 U. S. 134, 143 (1932).

⁴⁰ *American Tel. & Tel. Co. v. United States*, 299 U. S. 232, 237 (1936).

APPENDIX A

ANALYSIS OF THE \$2,741,591.66 BY YEARS AND ACQUISITIONS

ACQUISITION No	NAME OF COMPANY DIRECTLY CONVEYING PROPERTY TO PACIFIC	DATE OF ACQUISITION ¹	AMOUNT ESTABLISHED IN ACCOUNT 1005 APPLICABLE TO THE ACQUISITION (dollars)	% OF TOTAL	RECORD REFERENCES
1	Columbia Power & Light Company Yakima-Pasco Power Company Astoria Electric Company	1909 or 1910	\$1,321,601.45	48.0	3 R., Ex. 17, Rev. Statement B, p. 17, 1R. 168, 2R. 440 3 R., Ex. 17, Rev. Statement B, p. 18, 1R. 168, 2R. 440 3 R., Ex. 17, Rev. Statement B, p. 19, 1R. 168, 2R. 440
2.	Husum Power Company	1911	23,759.81	0.8	3 R., Ex. 17, Rev. Statement B, p. 21, 1R. 170, 2R. 440
3.	The Prosser Power Company and Prosser Water Company	1911	5,738.56	0.2	3 R., Ex. 17, Rev. Statement B, p. 21, 1R. 170-171, 2R. 440
4	The Klickitat Light & Power Company	1911	1,080.35	-	3 R., Ex. 17, Rev. Statement B, p. 26, 2R. 440
5.	Hood River Light & Power Company	1911	164,979.19	6.0	3 R., Ex. 17, Rev. Statement B, p. 26, 1R. 171, 2R. 440
6.	Tucannon Power Company	1911	39,260.64	1.4	3 R., Ex. 17, Rev. Statement B, p. 27, 1R. 171, 2R. 440
7.	Dayton Electric Company	1911	40,648.17	1.5	3 R., Ex. 17, Rev. Statement B, p. 28, 1R. 171, 2R. 440
8.	Waiteburg Electric Light Company	1911	45,873.41	-0.2	3 R., Ex. 17, Rev. Statement B, p. 29, 2R. 440
9.	Reservation Electric Company	1911	9,158.42	0.3	3 R., Ex. 17, Rev. Statement B, p. 29, 2R. 440
	Sub-Total 1909-1911		\$1,600,353.18	58.0	
10.	Hydro-Electric Company	1915	115,718.63	4.2	3 R., Ex. 17, Rev. Statement B, p. 31, 1R. 172-173, 2R. 440
11.	Seaside Light and Power Company	1916	21,683.76	0.8	3 R., Ex. 17, Rev. Statement B, p. 32, 1R. 174, 2R. 440
12.	Gestuart Park Company	1916	77.60	-	3 R., Ex. 17, Rev. Statement B, p. 33, 2R. 440
	Sub-Total 1915-1916		\$137,479.99	5.0	
13.	Inland Power & Light Company	1923 ²	1,085,512.23	39.5	3 R., Ex. 17, Rev. Statement B, pp. 37-41, 2R. 440
14.	Cannon Beach Electric Company	1928	1,512.62	0.6	3 R., Ex. 17, Rev. Statement B, p. 34, 1R. 174, 2R. 440
	Sub-Total 1923-1928		\$1,087,024.85	40.1	
15.	Connell Power & Light Company	1935	12.26	-	3 R., Ex. 17, Rev. Statement B, p. 44, 2R. 440
	Sub-Total 1935		\$12.26		
	Adjustments Applicable to Acquisitions: Gross Plant Additions		14,177.27	0.5	2R. 440
	Adjustments by Commissions' Staffs Accepted by Pacific		*(97,455.89)	-3.6	2R. 440
	Total Acquisitions Adjustments		\$2,741,591.66	100.0	2R. 440

¹ The property acquired was in existence long before the dates of acquisition. Some of the property was in existence as far back as 1885 (1 R. 126).

² Although the transfer to Pacific by Inland was made in 1914, the property had been acquired by Inland in 1923. The acquisition adjustment relates to the 1923 transaction since they were arm's-length transfers as delineated from the 1920 transfer, which was between affiliates.

³ These figures are taken from Column 7 of the exhibit having no number which is included in Volume 3 of the printed record following Exhibit 17.

⁴ Credit figure.

APPENDIX B

COMMISSION ORDERS AUTHORIZING THE AMORTIZATION OF AMOUNTS CLASSIFIED IN ACCOUNT 100 5, ELECTRIC PLANT ACQUISITION ADJUSTMENTS

<i>Name of Company</i>	<i>Docket No.</i>	<i>Date of Order</i>
Georgia Power Company	IT-5682	Feb. 27, 1941
New Mexico Power Company	-	June 3, 1941
Iowa Union Electric Company	IT-5685	Nov. 6, 1941
Northwestern Wisconsin Electric Company	IT-5716	Nov. 12, 1941
Wisconsin Central Utilities Company	IT-5717	Nov. 12, 1941
Potomac Electric Power Company	IT-5728	Dec. 30, 1941
Blackstone Valley Gas & Electric Company	-	Jan. 13, 1942
El Paso Electric Company (Texas)	IT-5733	Jan. 20, 1942
Northwestern Illinois Utilities	IT-5759	Jan. 27, 1942
Missouri Utilities Company	IT-5768	Feb. 3, 1942
Pennsylvania Electric Company	IT-5760	Feb. 18, 1942
Yamhill Electric Company	-	May 19, 1942
Duke Power Company	-	June 2, 1942
Kansas City Power & Light Company	IT-5737	June 12, 1942
Portland General Electric Company	IT-5779	July 31, 1942
Missouri Service Company	IT-5778	Aug 11, 1942
Gulf States Utilities Company Re Raton Rouge Electric Com- pany	IT-5787	Aug 18, 1942
Wisconsin Michigan Power Company	IT-5722	Oct. 6, 1942
Montana-Dakota Utilities Company	-	Oct 13, 1942
Benton County Utilities Corporation	IT-5744	Oct 20, 1942
Indiana Service Corporation	-	Jan. 5, 1943
Central Vermont Public Service Corporation	IT-5807	Jan. 5, 1943
Cincinnati Gas & Electric Company, The	-	Jan. 13, 1943
Delaware Power & Light Company	IT-5810	Jan. 13, 1943
Southern California Edison Company, Ltd.	-	Jan. 19, 1943
Sioux City Gas and Electric Company	IT-5809	Apr 20, 1943
Idaho Power Company	IT-5827	May 18, 1943
West Virginia Light, Heat and Power Company	IT-5823	June 9, 1943
Twin State Gas & Electric Company, The	IT-5843	Aug 3, 1943
Gulf Power Company	-	Sept. 7, 1943
Kentucky and West Virginia Power Company, Inc.	IT-5752	Sept. 7, 1943
Virginia Public Service Company	-	Sept. 21, 1943
Wheeling Electric Company	-	Sept. 21, 1943

APPENDIX C

PACIFIC POWER & LIGHT COMPANY

INCOME ACCOUNT FOR THE 12 MONTHS ENDED DECEMBER 31, 1940
REFLECTING THE AMORTIZATION OF ACCOUNT 100.5 THROUGH ACCOUNT 505 AND ACCOUNT 537

	AMORTIZATION THROUGH ACCOUNT 505	AMORTIZATION THROUGH ACCOUNT 537	DIFFERENCE \$ -
Operating Revenues	\$5,789,684.01	\$5,789,684.01	-
Operating Revenue Deductions:			
Operating expenses	2,732,522.50	2,732,522.50	-
Property retirement reserve appropriation	600,000.00	600,000.00	-
Amortization of limited-term utility investment	134.01	134.01	-
Amortization of utility plant acquisition adjustments	\$74,159.17	-	274,159.17
Taxes	883,103.90	883,103.90	-
Total operating revenue deductions	4,489,919.58	4,215,760.41	274,159.17
Net operating revenues	1,299,764.43	1,573,923.60	274,159.17
Income from Utility Plant Leased to Others	221,301.80	221,301.80	-
Utility operating income	1,521,066.23	1,795,225.40	274,159.17
Other Income:			
Revenues from lease of other physical property	536.00	536.00	-
Interest revenues	348,245.00	348,245.00	-
Miscellaneous nonoperating revenues	1,083.67	1,083.67	-
Nonoperating revenue (deductions)	(10,434.46)	(10,434.46)	-
Total other income	339,430.21	339,430.21	-
Gross income	1,860,496.44	2,134,655.61	274,159.17
Income Deductions:			
Interest on long-term debt	1,025,000.00	1,025,000.00	-
Amortization of debt discount and expense	8,132.40	8,132.40	-
Interest on debt to associated companies	167,670.00	167,670.00	-
Other interest charges	21,441.14	21,441.14	-
Interest charged to construction (credit)	(429.80)	(429.80)	-
Miscellaneous amortization	-	274,159.17	(274,159.17)
Miscellaneous income deductions	59,262.56	59,262.56	-
Total income deductions	1,281,076.30	1,553,235.47	(274,159.17)
Net income transferred to earned surplus	\$579,420.14	\$579,420.14	-

APPENDIX D

Excerpts from Federal Power Act (16 U. S. C. A., Secs. 791 et seq.):

SECTION 201. (a) It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this Part and the Part next following and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this Part and the Part next following, over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

(c) For the purpose of this Part, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) The term "sale of electric energy at wholesale" when used in this Part means a sale of electric energy to any person for resale.

(e) The term "public utility" when used in this Part or in the Part next following means any person who owns or operates facilities subject to the jurisdiction of the Commission under this Part.

(f) No provision in this Part shall apply to, or be deemed to include, the United States, a State or any political subdivision of a State, or any agency, authority, or instrumentality of any one or more of the foregoing, or any corporation which is wholly owned, directly or indirectly, by any one or more of the foregoing, or any officer, agent, or employee of any of the foregoing acting as such in the course of his official duty, unless such provision makes specific reference thereto.

SECTION 208. (a) The Commission may investigate and ascertain the actual legitimate cost of the property of every public utility, the depreciation therein, and, when found necessary for rate-making purposes, other facts which bear on the determination of such cost or depreciation, and the fair value of such property.

(b) Every public utility upon request shall file with the Commission an inventory of all or any part of its property and a statement of the original cost thereof, and shall keep the Commission informed regarding the cost of all additions, betterments, extensions, and new construction.

SECTION 301. (a) Every licensee and public utility shall make, keep, and preserve for such

periods such accounts, records of cost-accounting procedures, correspondence, memoranda, papers, books, and other records as the Commission may by rules and regulations prescribe as necessary or appropriate for purposes of the administration of this Act, including accounts, records, and memoranda of the generation, transmission, distribution, delivery, or sale of electric energy, the furnishing of services or facilities in connection therewith, and receipts and expenditures with respect to any of the foregoing: *Provided, however,* That nothing in this Act shall relieve any public utility from keeping any accounts, memoranda, or records which such public utility may be required to keep by or under authority of the laws of any State. The Commission may prescribe a system of accounts to be kept by licensees and public utilities and may classify such licensees and public utilities and prescribe a system of accounts for each class. The Commission, after notice and opportunity for hearing, may determine by order the accounts in which particular outlays and receipts shall be entered, charged, or credited. The burden of proof to justify every accounting entry questioned by the Commission shall be on the person making, authorizing, or requiring such entry, and the Commission may suspend a charge or credit pending submission of satisfactory proof in support thereof.

(b) The Commission shall at all times have access to and the right to inspect and examine all accounts, records, and memoranda of licensees and public utilities, and it shall be the duty of such licensees and public utilities to furnish to the Commission, within such reasonable time as the Commission may order, any information with respect thereto which the Commission may by order require, including copies of maps, contracts, reports of engineers, and other data, records, and papers, and to

grant to all agents of the Commission free access to its property and its accounts, records, and memoranda when requested so to do. No member, officer, or employee of the Commission shall divulge any fact or information which may come to his knowledge during the course of examination of books or other accounts, as hereinbefore provided, except insofar as he may be directed by the Commission or by a court.

(c) The books, accounts, memoranda, and records of any person who controls, directly or indirectly, a licensee or public utility subject to the jurisdiction of the Commission, and of any other company controlled by such person, insofar as they relate to transactions with or the business of such licensee or public utility, shall be subject to examination on the order of the Commission.

SECTION 304. (a) Every licensee and every public utility shall file with the Commission such annual and other periodic or special reports as the Commission may by rules and regulations or order prescribe as necessary or appropriate to assist the Commission in the proper administration of this Act. The Commission may prescribe the manner and form in which such reports shall be made, and require from such persons specific answers to all questions upon which the Commission may need information. The Commission may require that such reports shall include, among other things, full information as to assets and liabilities, capitalization, net investment, and reduction thereof, gross receipts, interest due and paid, depreciation, and other reserves, cost of project and other facilities, cost of maintenance and operation of the project and other facilities, cost of renewals and replacement of the project works and other facilities, depreciation, generation, transmission, distribution, delivery, use, and sale of electric energy. The Commission may require any such person to make ade-

quate provision for currently determining such costs and other facts. Such reports shall be made under oath unless the Commission otherwise specifies.

(b) It shall be unlawful for any person willfully to hinder, delay, or obstruct the making, filing, or keeping of any information, document, report, memorandum, record, or account required to be made, filed, or kept under this Act, or any rule, regulation, or order thereunder.

SECTION 309. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this Act. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this Act; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours.

SECTION 313. (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this Act to which such person, State,

municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this Act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the Circuit Court of Appeals of the United States for any circuit wherein the licensee or public utility to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do.

The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

(c) The filing of an application for rehearing under subsection (a) shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

